

TCG's Basic Strategy

Identify and serve un-served or under-served local telecommunications markets:

- ▶ **Provide local telecommunications services that are not provided at all or are not provided well by local exchange companies.**
- ▶ **Serve market segments that local exchange carrier cannot serve at all or cannot serve well.**

What Business Is TCG Really In?

BEING "NOT THE PHONE COMPANY"

or

BEING "THE OTHER LOCAL PHONE COMPANY"

Reason: It is TCG's permanent and substantial competitive advantage that the historic "phone company" can NEVER match.

TCG's Traditional Users

Characteristics:

- ▶ Large
- ▶ Telecommunications intensive/dependent
- ▶ Technically sophisticated

Major Segments:

- ▶ Interexchange carriers
- ▶ Brokerage/Financial services
- ▶ Information services
- ▶ Insurance
- ▶ Entertainment
- ▶ Retail

TCG's Services

U.S. and CCITT Standard Private Line Services:

- ▶ DS3: 44.736 Mbps
- ▶ DS2: 6.312 Mbps
- ▶ DS1: 1.544 Mbps
- ▶ E1: 2.048 Mbps
- ▶ "Fractional T1": 64, 128, 256, 512, 768 Kbps
- ▶ DS0: Voice Grade and Digital Data services
- ▶ Video: Broadcast and Private
- ▶ LanLink

Enhanced Switched Services:

- ▶ Local Calling
- ▶ TeleXpress PBX Access Trunks
- ▶ TCG Centrex
- ▶ Facility Management
 - PBX Networks
- ▶ Shared Tenant Services
- ▶ Payphones

Why Choose TCG?

– Operational Security

TCG Provides Operational Security

Physical diversity (route, switch)

- ▶ **LEC can provide (at high cost)**

Vendor diversity

- ▶ **LEC cannot provide**

Operational Security

"...Businesses that cannot afford telecommunications service interruptions often purchase service from both the LEC and CAP to achieve what is often referred to as operational security. The concept is that taking service from two independent local networks provides a level of reliability that cannot be achieved by a single network".

Source: Texas PUC "Scope of Competition"
Report to the Texas Legislature,
Jan 1993 at 29

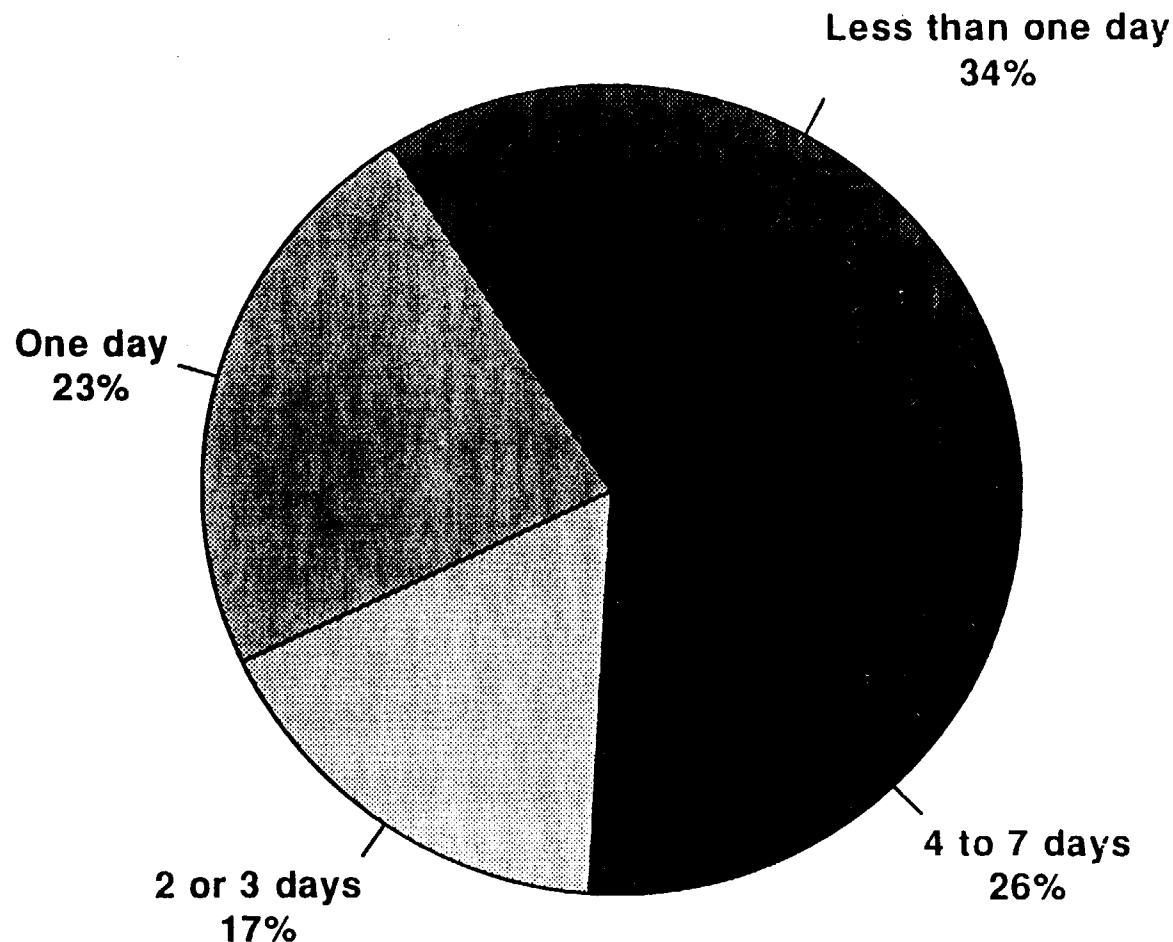
Vendor Diversity and "Disaster Avoidance" Create New Market

"As large business users concentrate more traffic into high capacity circuits, they grow more concerned about the impact of network failure. Consequently, AAP's [Alternative Access Providers] have found a new market in providing anxious customers with diverse and redundant networks as insurance against failure or disaster."

Source: "Inside Line" (Pacific Telesis' "News Update for the Financial Community") June 17, 1991 (Emphasis Added)

Disaster Avoidance Is Not Only A "Big Business" Concern

Number of Days Small and Medium Sized Business Could
Survive Without ANY Telephone Service



Source: Continuous Communications: Enhancing Network Reliability Through Cooperation/Report of the New York City Mayor's Task Force on Telecommunications Network Reliability, November 1991 (Fig. 5-2)

Uncompetitive Telecom Means Uncompetitive Businesses

"The loss of any portion of our telecommunications system or the inability to receive or place calls could easily result in the direct loss of millions of dollars in revenue. The indirect consequences would include the loss of confidence by our customers, which would no doubt cause a diversion of business to our competitors, many of which are located in cities such as Chicago, Boston and New York. Those cities... have a more secure local telecommunications infrastructure, due largely to regulatory policies."

"Second Full Hearing on California's Telecommunications Infrastructure," Testimony of Paul Evenson, Vice President, Montgomery Securities, (Cal. P.U.C. June 1, 1993)

Why Choose TCG?

- Strategic Security**

Strategic Security

"...The issue of strategic security arises when a LEC comes into direct competition with its largest customers. For example, a LEC may enter a market such as financial or information services, placing itself in competition with some of its customers who also provide these services."

Source: Texas PUC "Scope of Competition"
Report to Texas Legislature,
Jan 1993 at 20

TCG Provides Strategic Security

**LEC's Compete (or Are Planning to Compete)
With Their Biggest Customers**

- ▶ **Interexchange Carriers**
- ▶ **Financial Services**

TCG Doesn't Compete With Its Customers

- ▶ **Why buy essential components of your business from a competitor if a non-competitor provides equal (or better) service at similar prices?**

By Competing With Their Best Customers, LEC's Are Driving Major Users Off LEC Networks

"... LECs which adopt an adversarial strategy toward IXC's can expect to lose access revenues as IXC's leverage their relationships with users to divert traffic to ALTs."

Source: Competitive Assessment of the Market for Alternative Local Transport
Joseph Kramer, Deloitte & Touche, June, 1991

"... Finally, in the long run, [IXCs] and the local telcos see each other as major competitors and are trying to move away from being dependent on each other ... The long distance carriers have begun to move some of their business away from the traditional local telephone companies to the ALTs."

Source: "Competition is Emerging in the U.S. Telephone Market"
Joel Gross, Donaldson, Lufkin & Jenrette Securities Corporation, June 7, 1991

LECs Cannot Satisfy All User Needs

"...Just as operational security can be provided only by a carrier other than the LEC, strategic security can be provided by a carrier that is not in competition with its customers."

Source: Texas PUC "Scope of Competition"
Report to Texas Legislature,
Jan 1993 at 20

Requirements for Local Telecommunications Competition

- ▶ **Technical and operational feasibility**
 - **Interconnections, unbundling**
- ▶ **Legality**
 - **PUC authorization**
- ▶ **Economic viability**
 - **Market demand**
 - **Interconnection costs**
 - **Universal service**

Essential Interconnections For Effective Local Exchange Competition

- 1. Central Office interconnection arrangements
(Collocation)**
- 2. Connections from the CO interconnection
arrangement to unbundled LEC network
elements**
- 3. Seamless physical integration into LEC
interoffice networks**

Essential Interconnections For Effective Local Exchange Competition

- 4. Seamless logical/operational integration into LEC signalling networks**
- 5. Equal status in and control over LEC network databases and support systems**
- 6. Equal rights to and control over number resources in the North American Numbering Plan, including direct assignment of central office codes**

Essential Interconnections For Effective Local Exchange Competition

- 7. Local telephone number portability**
- 8. Reciprocal inter-carrier compensations
arrangements for the exchange of
traffic between LEC and rival local
carriers**
- 9. Cooperative practices and procedures**

Access to Customers and Rights of Way Is Critical Prerequisite

"Metropolitan or urban carriers have faced significant barriers to market entry because they must usually negotiate separately with each building owner, as well as obtain municipal franchises and other permits and meet state legal regulatory requirements."

Source: FCC Fiber Deployment Update, March 1992

Critical Elements Of USA

Subsidize Customers, Not Carriers

Equal Access to the Subsidies

**All Subsidized Services Open to Competition
(with necessary unbundling and interconnection)**



Teleport Communications Group, Inc. **Leading The Charge For Competitive Local Telephone Services** **Recommendation: BUY (OTC#-TCGI-\$18 1/8)**

Telecommunications

August 9, 1996

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Price 08/09/96	Price Target (12-18 month)	Indicated Dividend	Dividend Yield	Market Cap. (\$ in millions)	52-Week Price Range
\$18 1/8	\$28.00	Nil.	NM	\$2,880.1	\$19 1/2-\$14 1/8
Revenue (\$ in millions)					
	Q1	Q2	Q3	Q4	Year
1995A	\$39.7	\$43.2	\$47.6	\$54.4	\$184.9
1996E	\$58.1A	\$65.1A	\$72.5	\$80.8	\$153.3
1997E					\$412.5
EBITDA (\$ in millions)					
	Q1	Q2	Q3	Q4	Year
1995A	(\$1.7)	\$0.2	\$0.0	\$2.1	\$0.6
1996E	\$0.9A	\$2.4A	\$2.2	\$2.4	\$4.6
1997E					\$13.6
Earnings Per Share					
	Q1	Q2	Q3	Q4	Year
1995A	(\$0.07)	(\$0.07)	(\$0.08)	(\$0.12)	(\$0.34)
1996E	(\$0.17)A	(\$0.16)A	(\$0.24)	(\$0.26)	(\$0.84)
1997E					(\$1.32)
Capitalization (\$ in millions)			Operating Statistics		
March 31, 1996			June 30, 1996		
Long-Term Debt	987.01	54.3%	Total Markets		55
Shareholders Equity	829.30	45.7%	Buildings Connected		6,037
Total	\$ 1,816.31	100.0%	Route Miles		5,770
			Fiber Miles		286,009
Shares Outstanding		158.9	VGEs (Millions)		3.36
Market Capitalization		\$2,880.1	Central Office Switches		21
Book Value Per Share		\$5.22	Employees		1,697

Summary & Recommendation

We initiated coverage of Teleport Communications Group, Inc. on July 23, 1996, with a **BUY** rating and a 12-18 month price target of \$28. TCG is one of the best positioned companies to capitalize on the unprecedented opportunity created by the deregulation of the local telecommunications industry. Teleport is the oldest and largest provider of competitive local exchange services in the U.S., currently serving 6,037 buildings in 55 markets with 5,770 network route miles. TCG's network footprint is unmatched by any CLEC, positioning the company to realize significant operating leverage as it generates incremental revenue. We view TCG as one of the premier competitors in the group and probably the highest quality investment opportunity in the group on a risk versus return basis. With over one billion dollars already invested in its fiber networks, a significant presence in all the major cities in the U.S., numerous strategic relationships, positive cash flow (no other CLEC offers this), and an unprecedented deregulatory environment, TCG should be considered a key holding in any growth-oriented investment portfolio.

¹Deutsche Morgan Grenfell/C. J. Lawrence co-managed the June 27, 1996 offering of 26,320,000 shares of Class A common stock of Teleport Communications Group, Inc.
 # Deutsche Morgan Grenfell/C. J. Lawrence Inc. makes a market in this security.

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I. KEY INVESTMENT POINTS

1. ***Initiated Coverage With A BUY Rating.*** We initiated coverage of TCG on July 23, 1996, with a **BUY** rating and a 12-18 month price target of \$28. As the oldest and largest of the competitive local exchange carriers (CLECs), we believe that TCG offers investors a unique opportunity to capitalize on the historic growth opportunity that has developed in the competitive local market, with a high degree of potential upside and a low degree of corresponding risk.
2. ***Federal Legislation Paves The Way For TCG's Growth.*** The largest catalyst for TCG's growth was the passage of the Telecommunications Act of 1996. The Act and the August 1, 1996, FCC rule-making procedure clearly laid the groundwork for TCG to leverage its vast fiber network and significantly expand its target market while dramatically reducing the cost of interconnecting with the incumbent local telcos.
3. ***TCG Is At An Inflection Point In Its Growth Curve.*** With its access to capital dramatically expanded by its \$1.3 billion financing and newfound independence in the wake of the termination of the wireline portion of the Sprint Telecommunications Venture, the stage is set for TCG to significantly expand its sales efforts on the heels of landmark legislative victories that have dramatically expanded its market opportunity.
4. ***Network Deployment Unmatched By Any CLEC.*** TCG has fiber-based networks in operation or under development in 55 metropolitan areas today with a total of 5,770 network route miles and 21 class five switches. TCG serves a total of 6,037 buildings in its markets and 3.4 million voice grade equivalent circuits (VGEs). The company's network deployment is by far the most expansive of any of the CLECs.
5. ***Cable Relationships Provide A Competitive Advantage.*** As a result of its relationship with four of the largest cable operators, TCG has a significant speed to market and a cost structure advantage over its industry peers. These relationships offer TCG a significant opportunity to leverage the vast rights-of-way and existing fiber of its cable partners in order to deploy its networks in a cost-effective and expedient manner.
6. ***Relationships With IXC's Could Generate Strong Growth.*** TCG has strategic and contractual relationships with all of the top long distance carriers and has master service agreements with the top eight, including AT&T, MCI, Sprint, WorldCom and LCI. The company has a nationwide preferred vendor relationship with AT&T for the provision of special and switched access, and a local dialtone service trial is underway.
7. ***Strong And Seasoned Management Team At The Helm.*** A key contributor to TCG's development has been the leadership of a strong management team made up of seasoned professionals from the competitive access, long distance, and cable industries. TCG's management founded the CLEC industry and have adeptly capitalized on the opportunities in the competitive local market during the past 13 years.
8. ***Expect Significant Penetration Of TCG's Addressable Market.*** We estimate that TCG's year 2005 addressable market opportunity will be \$55 billion. Based on our conservative expansion and capital deployment models, we estimate that TCG will be able to penetrate approximately 6.6% of its market opportunity in the year 2005, generating revenue of approximately \$3.6 billion.
9. ***Market Penetration Aided By Unique BizTel Relationship.*** We expect that TCG's market penetration and cost structure will be significantly impacted by its unique relationship with BizTel, a 38 GHz fixed wireless operator with licenses in 156 markets covering geographic areas with a population of 175 million. TCG has a 49.9% stake in BizTel, with the option to increase its stake to 74.9%.
10. ***TCG Offers Investors A Compelling Value.*** TCG is very attractive on the basis of its valuation alone, as it trades at a significant discount to its peers and to our target price of \$28. By just about any standard of comparison, TCG trades at a discount to the other CLECs, while offering what we believe is a premium in terms of network footprint, financial structure, strategic relationships, and most importantly, financial results.



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III. INVESTMENT VIEWPOINT

Initiated Coverage With A BUY Rating. We initiated coverage of Teleport Communications Group, Inc. on July 23, 1996, with a **BUY** rating and a 12-18 month price target of \$28. Teleport is the oldest and largest provider of competitive local exchange services in the U.S., currently serving 6,037 buildings in 55 markets with 5,770 network route miles. TCG has evolved from a competitive access provider (CAP) to a full-fledged competitive local exchange carrier (CLEC) that markets itself as *The Other Local Phone Company*. TCG provides a broad variety of standard and enhanced voice, data and video services to its local exchange customers over its fully redundant broadband network, enhanced by superior customer service and a commitment to do whatever it takes in order to fulfill a customer's communications needs. TCG differentiates itself from its peers by its strict local service focus, the unmatched size and scope of its operations, and through its high quality and innovative service offerings, which target both business end users and telecommunications carriers.

TCG Is Best Positioned Among The CLECs. We remain convinced that the greatest beneficiaries of the landmark Telecommunications Act of 1996 will be the aggressive new competitors in the local telephone arena. In fact, the principal purpose of legislation was clearly to end the monopolistic structure that has impeded new product development, customer service, and consumer choice while generating substantial cash flow and profitability for the legislatively-defined incumbents. In recognition of that opportunity, we have been quite bullish on many of the CLECs, both big and small. In that context, we view TCG as one of the premier competitors in the group and probably the highest quality investment opportunity on a risk-versus-return basis. With over one billion dollars already invested in its fiber networks, a significant presence in all the major cities in the U.S., numerous strategic relationships, positive cash flow (no other CLEC offers this), and an unprecedented deregulatory environment, TCG should be considered a key holding in any growth-oriented investment portfolio.

Company Overview. Founded in 1983, TCG is the nation's largest competitive local service provider (CLEC), with fiber optic networks in operation or under development in 55 markets throughout 26 states. The company serves its markets with more than 5,770 route miles of broadband fiber optic plant in service and 21 class five digital switches. TCG's fiber optic network footprint is supplemented by a 49.9% stake in BizTel, a fixed-wireless operator that owns 38 GHz broadband licenses in 156 metropolitan areas covering a population of 175 million. TCG has developed from a pure-play access provider into a competitive local service provider which provides voice, data, video transport and network services to customers in government, business, and industry. As a full-service CLEC, the company also provides pay phone service and has the potential to provide residential telephone service in multi-tenant apartment buildings. TCG differentiates itself from other CAPs through its service offerings, which target carriers and end users, including both residential and business customers as well as telecommunications carriers. The company posted 1995 revenue of \$184.9 million with positive EBITDA of \$0.6 million, and we estimate that TCG can attain revenue of \$3.6 billion by the year 2005 with corresponding EBITDA margins of 35%.

Company History. TCG was founded in 1983 when Bob Annunziata convinced Merrill Lynch, his employer at that time, of the incredible opportunity in the competitive access market. TCG founded the CAP industry and was the first to recognize the importance of transitioning from a pure play competitive access provider (CAP) to a full-service competitive local exchange carrier (CLEC). With that recognition, TCG has been at the forefront of the regulatory struggle to open all aspects of the local exchange, and was instrumental in establishing the 14-point checklist included in the Telecommunications Act of 1996. Merrill Lynch sought outside investors for TCG in 1991 and sold an equity stake to Cox Communications. The following year, TCI, Comcast and Continental Cablevision acquired the balance of TCG, providing TCG with the capital and strategic relationships necessary to significantly accelerate its growth. On October 25, 1994, TCI, Sprint, Cox, and Comcast announced the historic but short-lived Triple Play venture, to which TCG was to be contributed. However, the wireline portion of the venture ultimately deteriorated and with the announcement of its demise on February 1, 1996, the door was opened for TCG to go public as an independent entity.

Management Team. The driving force in TCG's development has been the leadership of a management team made up of strong and seasoned professionals from the competitive access, long distance, and cable industries.